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No. 93

In the Supreme Court of the United States

OCTOBER TERM, 1929

ANITA H. COOPER, PETITIONER

v.

THE UNITED STATES

ON WRIT OF CERTIORARI TO THE COURT OF CLAIMS

BRIEF FOR THE UNITED STATES

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OPINION BELOW

There is no written opinion by the Court of Claims. That court made findings of fact and conclusion of law. (R. 11–13.)

JURISDICTION

The judgment of the Court of Claims was entered on May 6, 1929. (R. 13.) Petition for writ of certiorari was filed May 17, 1929 (R. 13), and allowed October 14, 1929 (R. 15). The jurisdiction of this Court is invoked under Section 3 (b) of the Act of February 13, 1925.

QUESTION PRESENTED

Property was given to petitioner and sold by her within the taxable year contemplated by the Revenue Act of 1921, but prior to the date upon which it was enacted. Section 202 (a) (2) of that Act provides that the basis for computing gain upon the sale of property acquired by gift after December 31, 1920, shall be the cost of the property to the donor. Does this section apply to a sale of such property occurring during the taxable year prior to the passage of the Act, and, if so, does it deprive petitioner of property without due process of law?

STATUTE INVOLVED

Revenue Act of 1921, c. 136, 42 Stat. 227, 229, 237, 238, 271:

TITLE II.—INCOME TAX

> SEC. 202. (a) That the basis for ascertaining the gain derived or loss sustained from a sale or other disposition of property, real, personal, or mixed, *acquired after February 28, 1913,* shall be the cost of such property; EXCEPT that—
>
> ~~(1) Inventory property basis last inventory.~~
>
> (2) In the case of such property, *acquired by gift after December 31, 1920,* the basis shall be the same as that which it would have in the hands of the donor or the last preceding owner by whom it was not acquired by gift. If the facts necessary to determine such basis are unknown to the donee, the Commissioner shall, if possible, obtain such

facts from such donor or last preceding owner, or any other person cognizant thereof. If the Commissioner finds it impossible to obtain such facts, the basis shall be the value of such property as found by the Commissioner as of the date or approximate date at which, according to the best information the Commissioner is able to obtain, such property was acquired by such donor or last preceding owner. *In the case of such property acquired by gift on or before December 31, 1920,* the basis for ascertaining gain or loss from a sale or other disposition thereof shall be the fair market price or value of such property at the time of such acquisition;

* * * * *

SEC. 213. That for the purposes of this title (except as otherwise provided in section 233) the term "gross income"—

(a) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including in the case of the President of the United States, the judges of the Supreme and inferior courts of the United States, and all other officers and employees, whether elected or appointed, of the United States, Alaska, Hawaii, or any political subdivision thereof, or the District of Columbia, the compensation received as such), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, *or sales, or dealings in property, whether real or personal, growing* out of the ownership

or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. The amount of all such items (except as provided in subdivision (e) of section 201) shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of section 212, any such amounts are to be properly accounted for as of a different period; but

(b) Does not include the following items, which shall be exempt from taxation under this title:

* * * * *

(3) The value of property acquired by gift, bequest, devise, or descent (but the income from such property shall be included in gross income);

* * * * *

SEC. 263. That this title shall take effect as of January 1, 1921.

STATEMENT

The facts found by the Court of Claims are as follows:

The petitioner, Anita H. Cooper, is a citizen of the United States and a resident of the City of New York. (R. 11.)

In 1918 petitioner's husband acquired 380 shares of the stock of the New York County National

Bank at $113.50 per share. On November 1, 1921, petitioner received by absolute gift from her husband this stock, which she sold on November 7, 1921, at a price of $210 per share. The value at the time of the gift was also $210 per share. (R. 12.)

Petitioner reported in her income tax return for the year 1921 as income, under Section 202 (a) (2) of the Revenue Act of 1921, $36,670, the difference between the cost of said shares to her husband and the price received by her. Petitioner was required to pay $8,474.90 more in taxes than she would have been required to pay had she used as the basis for determining gain the fair market value of the shares at the time they were acquired by her. On September 15, 1926 she filed a claim for refund of this amount. On November 30, 1926, the Commissioner of Internal Revenue rejected this claim. (R. 11, 12.)

Suit was thereupon commenced in the Court of Claims for recovery of the amount. (R. 5.) Upon hearing, the petition was dismissed. (R. 13.) Petition for writ of certiorari followed.

SUMMARY OF ARGUMENT

It is settled that upon the sale of property acquired by gift the donee may properly be required to account for all of the profit over the cost to the donor. It is clear from the statute that it was intended to include in the measure of income all gains received in the calendar year during which the sale here involved took place, including any received before its passage.

The only remaining question is whether such limited retroactivity transcends the power of Congress. With respect to income taxes this Court has repeatedly held that the fact that such a statute may have in some respects a retroactive effect does not cause it to be beyond the power of Congress.

The decisions holding that certain statutes imposing excises upon particular transactions were invalid because of their retroactive effect are distinguishable. This tax was not imposed upon the transaction here involved but upon the net income of the entire period, which included the date of this transaction. The profit upon the particular transaction was included in the measure of the tax, and it is settled that things may be included in the measure of a tax which could not be directly taxed.

If the objection to this tax were upheld, it would be difficult to state a reason why Congress would not be also without power retroactively to increase rates and yet this power has been repeatedly exercised and upheld.

ARGUMENT

A TAX ON INCOME DERIVED FROM THE SALE OF A GIFT AND MEASURED BY THE INCREASE IN THE VALUE OF THE GIFT DURING THE SUCCESSIVE OWNERSHIP OF THE DONOR AND THE DONEE IS NOT VOID BECAUSE OF RETROACTIVITY

In *Taft* v. *Bowers,* 278 U. S. 470, this Court held that where property, the subject of a gift, was sold by the donee, all increase in its value occurring during the ownership of both the donor and the donee

was income to the donee, and subject to tax imposed by Section 202 (a) (2) of the Revenue Act of 1921.

The instant case is governed by the same statute which was involved in the *Taft case,* and differs from it only in that petitioner here received the gift and sold it prior to the enactment of the Act, although within the taxable year embraced by the Act.

In *Brushaber* v. *Union Pac. R. R.* 240 U. S. 1, 20, and *Lynch* v. *Hornby,* 247 U. S. 339, income-tax provisions of the Revenue Act of 1913, retroactive to March 1, 1913, were held to be valid. But, further, the application of the Revenue Act of 1913 to a taxpayer who had died between March 1, 1913, and the effective date of the Act has been held valid. *Brady* v. *Anderson,* 240 Fed. 665, certiorari denied, 244 U. S. 654. No subsequent income tax law has been held unconstitutional because of retroactivity. *United States* v. *McHatton,* 266 Fed. 602; *United States* v. *Boss & Peake Automobile Co.,* 285 Fed. 410, affirmed, 290 Fed. 167; *United States* v. *Updike,* 1 F. (2d) 550, affirmed, 8 F. (2d) 913, certiorari denied, 271 U. S. 661.

In the *Brushaber case* this Court held that the contention was foreclosed by the decision in *Stockdale* v. *Insurance Companies,* 20 Wall. 323, 331, where the Income Tax Act of June 30, 1864, as amended by the Act of July 14, 1870, c. 255, Section 17, 16 Stat. 256, 261, was held to be valid though retroactive.

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That decision was consistent with the earlier one in *Billings* v. *United States,* 232 U. S. 261, 282, where this Court held an excise tax on the use of a yacht to be valid, though applied retroactively. Thereafter, in *Hecht* v. *Malley,* 265 U. S. 144, 164, the capital-stock tax provisions of the Revenue Act of 1918 imposing a special excise tax with respect to doing business were applied retroactively to validate an earlier unauthorized collection.

The same rule has been generally applied in construing the retroactive effect of State and municipal taxing measures. See *Seattle* v. *Kelleher,* 195 U. S. 351, 359; *Wagner* v. *Baltimore,* 239 U. S. 207, 216.

Under the law as it existed prior to the Revenue Act of 1921, it was possible for the owner of property which had largely increased in value since his acquisition thereof to escape tax on this increase by a transfer *inter vivos* to another. To avoid resulting loss of revenue, Section 202 (a) (2) of the Revenue Act of 1921, *supra,* was adopted. This section did not create a new form of taxation, but merely broadened the scope of the previous Income Tax Acts. See *Taft* v. *Bowers, supra.* It is thus apparent that the tax in the instant case is one applying only to income and is not essentially different from that which this Court in the *Brushaber* and the *Hornby cases* held might validly be laid retroactively. To give effect to petitioner's contention would be to establish a rule that income derived from certain sources might validly be taxed retro-

actively, whereas other income, because derived from a different source, could not be so taxed.

Petitioner attempts to invoke the rule that a taxing statute should not be given a retrospective operation unless its words make that construction imperative (Pet. Br., p. 6), citing *Shwab* v. *Doyle,* 258 U. S. 529, and *Levy* v. *Wardell,* 258 U. S. 542. It is believed that the rule is not pertinent here.

Those cases arose under Section 202 of the Revenue Act of 1916, and raised the question as to the right of the Commissioner to include in the gross estate of a decedent, for estate-tax purposes, the value of property which the decedent had transferred in trust prior to the passage of that Act. In drawing that Act, Congress manifested no intention that it should be construed retroactively. This Court thereupon held that in the absence of such expressed intention the statute was not to be held retroactive.

In the Revenue Act of 1921, Section 263 specifically provides, "That this title shall take effect as of January 1, 1921." Section 202 (a) (2) of this Act is part of Title II, to which Section 263 refers. By Section 202 (a) (2) the question whether the basis of determining gain or loss from the sale of property acquired by gift was to be "that which it would have in the hands of the donor" or "the fair market price or value of such property at the time of such acquisition," was expressly made to depend on whether the property was so acquired after or before December 31, 1920.

We submit that there is no reasonable basis for a construction of the Act that Congress did not intend the basis of the cost to the doner to be applied in the case of property acquired by gift between December 31, 1920, and November 23, 1921, and sold before the latter date, and that such cases as *Shwab* v. *Doyle* and *Levy* v. *Wardell, supra,* have no application.

Petitioner then contends that if the language of the Act does require that Section 202 (a) (2) be applied, the section imposes an arbitrary and capricious exaction and is invalid under the due process clause of the Fifth Amendment. Petitioner relies upon *Nichols* v. *Coolidge,* 274 U. S. 531, *Blodgett* v. *Holden,* 275 U. S. 142, and *Untermyer* v. *Anderson,* 276 U. S. 440, to sustain this contention. The *Nichols case* arose under Section 402 (c) of the Revenue Act of 1918. Attempt was there made to include in a decedent's estate for estate tax purposes the value of property as to which decedent had made a transfer in trust prior to the enactment of the Act. This Court, in considering the effect of Section 402 (c), as applied retrospectively, said (p. 542):

> An excise is prescribed, but the amount of it is made to depend upon past lawful transactions, not testamentary in character and beyond recall. Property of small value transferred before death may have become immensely valuable, and the estate tax, swollen by this, may leave nothing for distribution.

From this it was concluded (pp. 542–543)—

> that Section 402 (c) of the statute here under consideration, in so far as it requires that there shall be included in the gross estate the value of the property transferred by a decedent prior to its passage merely because the conveyance was intended to take effect in possession or enjoyment at or after his death, is arbitrary, capricious, and amounts to confiscation.

It is believed that the above statement of this Court illustrates the distinction between the effect of the tax in that and the instant case. There the tax was an excise laid upon the doing of an act which had not been taxable when done. Here the tax is laid on income, which by the precise terms of the Sixteenth Amendment is subject to tax. There the tax was measured by the value of the estate which included the value of property previously transferred, but the tax was paid out of the estate remaining at death. Here the tax is measured by income actually received within the taxable year, and the payment is made by the recipient of that income.

In the *Blodgett case, supra,* the Circuit Court of Appeals for the Sixth Circuit certified to this Court the question whether Sections 319–324 of the Revenue Act of 1924 were unconstitutional in so far as they taxed transfers by gifts made prior to the date upon which that Act was approved. Those sections taxed the donor on the exercise of his right to make a gift. This Court answered the

question by saying that the Act did not apply to such gifts, four members of the Court being of the opinion that the Act was unconstitutional so far as it attempted to reach back, and four being of the opinion that there was no intention on the part of Congress to have it reach back. (See 276 U. S. 594.) The recent decision in *Bromley* v. *McCaughn* (No. 27, October Term, 1929, decided November 25, 1929) shows that this tax was an excise falling upon a particular transaction.

The *Blodgett case* was followed by *Untermyer* v. *Anderson, supra,* in which the same question was again presented. In the *Untermyer case* the additional question was raised whether the fact that the Act had been approved by both branches of Congress and was in conference at the time the gift was made, affected the case so far as the question of retroactivity was concerned. This Court there held (p. 445):

> that so far as applicable to bona fide gifts not made in anticipation of death and fully consummated prior to June 2, 1924, those provisions are arbitrary and invalid under the due process clause of the Fifth Amendment.

It is thus clear, as in the *Nichols case,* that the tax in the *Blodgett* and the *Untermyer cases* was an excise laid on the doing of an act, at some time in the past, whereas in the instant case the tax is on income received within the taxable year by the person called upon to pay the tax.

The decisions of this Court holding Federal taxing statutes invalid on account of retroactivity have all involved excises upon particular transactions. As this Court has said in *Knowlton* v. *Moore,* 178 U. S. 41, 88:

> Excises usually look to a particular subject, and levy burdens with reference to the act of manufacturing them, selling them, etc.

Unlike those excises, the tax in this case is not imposed upon any particular transaction. The tax is levied on the net income of a period. Not until after the date of the passage of this Act could it be determined whether any taxable net income had been earned. Although a gain might be realized from an individual transaction during the tax year, it could not be accurately said at the time that any taxable income had resulted, since the losses on other transactions might entirely offset the gain on the particular transaction and leave the individual without a net income. In industry it requires weeks and often months after the end of the year to examine an elaborate accounting system and compute what has been the year's income. The Act, therefore, was passed well within the period that taxpayers customarily require for a complete ascertainment of income and dealt with current events. In a similar situation this Court has referred to it as "limited retroactivity." *Brushaber* v. *Union Pac. R. R., supra,* p. 20. And in *Billings* v. *United States, supra,* p. 282, the statute was said to give the tax "in some respects a

retroactive effect." Accordingly, the tax here involved, if retroactive at all, is so classified merely because the measure of the tax includes the transactions of a period, a part of which has already passed. This Court has already said, in a case where the measure of a tax was the income from all sources, that it is no valid objection that this measure includes, in part, property which, as such, could not be directly taxed. *Flint* v. *Stone Tracy Co.*, 220 U. S. 107. Applying that doctrine to this case we submit that it is no valid objection to the tax that the measure includes, in part, gain from a transaction upon which a specific tax could not have been imposed retroactively.

It has been recognized that State income tax statutes may properly measure the tax by the income of a prior year. *Drexel & Co.* v. *Commonwealth*, 46 Pa. 31; *Glasgow* v. *Rowse*, 43 Mo. 479; *Income Tax Cases*, 148 Wis. 456, 514.

And it is well settled (*Maxwell* v. *Dow*, 176 U. S. 581, 602) that the language of a constitutional amendment should be read—

> in connection with the known condition of affairs out of which the occasion for its adoption may have arisen, and then to construe it, if there be therein any doubtful expressions, in a way so far as is reasonably possible, to forward the known purpose or object for which the amendment was adopted.

Since it appears that at the time of the adoption of the Sixteenth Amendment it was recognized that

income taxes could properly be measured by the income of a period a part of which had already passed, we submit that the Amendment authorizes income tax legislation of that kind.

All of the Federal Income Tax Acts have been retroactive in the sense that they applied to income for a period which began prior to the passage of the several Acts. We submit that in so far as income taxes are concerned, the practice in the past forecloses the contention that retroactivity brings an Act of Congress within the due-process clause of the Fifth Amendment.

If the objection made here to the measure of the tax is valid, it is difficult to frame a reason why it would not also apply to a retroactive increase in the rate of taxation. The power to increase rates retroactively has been recognized and in time of war Congress has repeatedly found it necessary.

As the Civil War progressed it was found necessary to levy (Resolution July 4, 1864) a special income tax for the whole year of 1863 (13 Stat. 417). This tax was imposed on incomes which had already been taxed at the rates established by a prior Act. In *Stockdale* v. *Insurance Companies, supra,* this Court said (p. 331): "No one doubted the validity of the tax or attempted to resist it."

The Act of June 30, 1864, c. 173, 13 Stat. 223, 281, applied to incomes for the calendar year 1864. The Act of March 3, 1865, c. 78, 13 Stat. 469, 479, ap-

plied to income for the entire year 1865 and raised the rates.

On June 13, 1898, Congress passed an Act to provide ways and means to meet the expenditures of the Spanish-American War (c. 448, 30 Stat. 448). By Section 3 a tax was imposed upon specified articles in addition to the tax already paid. In answer to the contention that the statute was unconstitutional, this Court said (*Patton* v. *Brady,* 184 U. S. 608, 619–620, 623):

> The obligation of the individual to the State is continuous and proportioned to the extent of the public wants. No human wisdom can always foresee what may be the exigencies of the future, or determine in advance exactly what the government must have in order "to provide for the common defence" and "promote the general welfare." Emergencies may arise; wars may come unexpectedly; large demands upon the public may spring into being with little forewarning; and can it be that having made provision for times of peace and quiet, the government is powerless to make a further call upon its citizens for the contributions necessary for unexpected exigencies?
>
> That which was possible in fact existed. A war had been declared. National expenditures would naturally increase and did increase by reason thereof. Provision by way of loan or taxation for such increased expenditures was necessary. There is in this legislation, if ever such a question could

arise, no matter of color or pretense. There was an existing demand, and to meet that demand this statute was enacted. The question, therefore, is whether Congressional provision must reach through an entire year and at the beginning finally determine the extent of the burden of taxes which can be cast upon the citizen during that year, with the result that if exigencies arise during the year calling for extraordinary and unexpected expenses the burden thereof must be provided for by way of loan, temporary or permanent; or whether there inheres in Congress the power to increase taxation during the year if exigencies demand increased expenditures. On this question we can have no doubt. Taxation may run *pari passu* with expenditure. The constituted authorities may rightfully make one equal the other. The fact that action has been taken with regard to conditions of peace does not prevent subsequent action with reference to unexpected demands of war. Courts may not in this respect revise the action of Congress. That body determines the question of war, and it may therefore rightfully prescribe the means necessary for carrying on that war. Loan or tax is possible. It may adopt either, or divide between the two. If it determines in whole or in part on tax, that means an increase in the existing rate or perhaps in the subjects of taxation, and the judgment of Congress in respect thereto is not subject to judicial challenge.

* * * * *

> Our conclusion, then, is that it is within the power of Congress to increase an excise as well as a property tax, and that such an increase may be made at least while the property is held for sale and before it has passed into the hands of the consumer; that it is no part of the function of a court to inquire into the reasonableness of the excise either as respects the amount, or the property upon which it is imposed.

More recently Section 1 of the Act of October 3, 1917, c. 63, 40 Stat. 300, imposed a tax upon income received in the calendar year 1917 in addition to the normal tax imposed by the Revenue Act of 1916. The Act of February 24, 1919, c. 18, Section 210, 40 Stat. 1057, 1062, provided increased rates beginning with the calendar year 1918 in lieu of the taxes imposed by the Revenue Acts of 1916 and 1917. This Act has been applied without question of its constitutionality. See, for example, *United States* v. *Robbins*, 269 U. S. 315.

Moreover, recent Revenue Acts have contained many provisions extending the basis for determining gross income, or restricting deductions therefrom, which have had the effect of retroactively increasing the burden of the tax. See, for example, War Revenue Act of 1917, c. 63, Secs. 3, 201, 40 Stat. 300, 301, 303; Revenue Act of 1918, c. 18, Secs. 240 (a), 326 (a) (4) and (5), 40 Stat. 1057, 1081, 1092; Revenue Act of 1921, c. 136, Secs. 201 (b), 245 (a) (5), 42 Stat. 227, 228, 262; Act of March

4, 1923, c. 294, 42 Stat. 1560; Revenue Act of 1926, c. 27, Sec. 231 (12), 44 Stat. 9, 40 (U. S. C. App. Title 26, Sec. 982); Revenue Act of 1928, c. 852, Sec. 23 (c), 45 Stat. 791, 799 (U. S. C. Sup. III, Title 26, Sec. 2023).

We submit that the decisions of this Court with respect to certain excises upon particular transactions have not so changed the situation that Congress is impotent in time of national need to meet exigencies by legislation retroactively increasing the rate of income tax or changing the basis of determining gain. As shown above, the statute in the instant case had a special justification in the necessity for preventing further tax avoidance.

It is an established proposition that Congress may retroactively ratify and legalize the collection of taxes which were unauthorized when collected. *United States* v. *Heinszen & Co.,* 206 U. S. 370. In *Charlotte Harbor Ry.* v. *Welles,* 260 U. S. 8, 11, it was said:

> And the power is necessary, that government may not be defeated by omissions or inaccuracies in the exercise of functions necessary to its administration.

It is not necessary to go so far to sustain the legislation involved in the case at bar. There is here involved only the power of Congress to impose upon income taxes which are retroactive over a limited period, and that power has been repeatedly upheld by this Court.

CONCLUSION

It is therefore submitted that the judgment of the Court of Claims should be affirmed.

Respectfully submitted.

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